STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

Illinois Commerce Commission	:	
On Its Own Motion	:	
	:	16-NOI-01
Notice of Inquiry Regarding the	:	
Regulatory Treatment of Cloud-	:	
Based Solutions	:	

REPLY COMMENTS OF THE JOINT SOFTWARE PROVIDER PARTIES TO THE NOTICE OF INQUIRY REGARDING THE REGULATORY TREATMENT OF CLOUD-BASED SOLUTIONS

I. Introduction

Advanced Energy Economy Institute, EnergyHub, EnergySavvy, EnerNOC, Inc., FirstFuel Software, Inc., Opower, Inc., Oracle, Inc., and Siemens, Inc., hereafter referred to as the "Joint Software Provider Parties", respectfully submit their Reply Comments in response to the Illinois Commerce Commission's ("Commission's) Notice of Inquiry Regarding the Regulatory Treatment of Cloud-Based Solutions ("NOI").[1] The Reply Comments were developed collectively by the Joint Software Provider Parties and should not be attributed to a particular member of the group. Contact information for each party that supports these comments can be found in Section III.

II. Reply Comments

The Joint Software Provider Parties are pleased to see overwhelming agreement among parties recognizing the potential benefits of cloud-based solutions and acknowledgment that ratemaking treatment can be a barrier to adoption of cloud-based software, and that there are straightforward ways to address this barrier.

[1] These Comments are filed and served pursuant to 2 Ill. Adm. Code 1700 Subpart D.

The Joint Software Provider Parties would like to highlight a few themes from the initial comments that were filed by various parties in the NOI:

First, every party acknowledges that significant benefits could be captured from cloud-based solutions, and these comments come from a broad range of utility and non-utility stakeholders. For instance, Ameren Illinois Company ("AIC") indicated that "Cloud computing provides a highly automated, dynamic, and cost-effective alternative for the acquisition and delivery of IT services." Commonwealth Edison Company ("ComEd") wrote that, "Offering solutions via the Cloud allows utilities more options to find efficient and cost effective solutions that benefit the grid and utility customers." For non-utility stakeholders, the People of the State of Illinois ("People") acknowledged the potential for "lower-cost, modern, efficient, and powerful cloud computing analytic solutions to utility operational needs" and the Utility Analytics Institute discussed the ability to realize "substantial customer service, operational and financial benefits of analytics solutions delivered via the cloud."

Second, utilities agree that current ratemaking treatment is a barrier to adoption of cloud-based software. For example, ComEd writes, "Recent accounting guidance clarification coupled with current ratemaking practice may result in adverse financial consequences when choosing a Cloud solution." Similarly, Nicor Gas Company ("Nicor Gas") writes, "Uncertainty in capitalization of any costs incurred in conjunction with cloud-based solutions tends to discourage a utility from considering cloud-based solutions, particularly if the similar on-premises solutions provide clarity in the desirable accounting treatment in ratemaking." North Shore Gas Company ("North Shore") and the Peoples Gas Light and Coke Company (Peoples Gas") (together, "NSG/PGL") comes to the same conclusion, writing, "Current ratemaking treatment is thus more favorable for on premises solutions and more appropriate in terms of the rate impact to customers." Finally, AIC echoes this theme, writing, "Current

Illinois ratemaking practice follows the GAAP rules. This current ratemaking practice is a disincentive for utilities to pursue cloud-based solutions, since such expenditures which were formerly capitalized, and provided a return on capital, are now expensed."

Third, utilities agree that there is no reasonable justification for this disincentive to exist. They make at least two arguments to support this claim. One argument is that solutions that meet the same need for the utility and deliver the same benefit for customers should be given the same accounting treatment. An example of this argument is in Nicor Gas's comments:

> "Generally speaking, Nicor Gas believes the similar investment in the equivalent solution should be accounted for the same way in ratemaking regardless of whether the solution is an on-premises solution or cloud-based solution. The current accounting focuses on ownership of the solution and timing of incurring costs, among other factors, in determining the proper accounting treatment. It is particularly the ownership aspect that differentiates the current accounting between on-premises solutions and cloud-based solutions. In ratemaking, Nicor Gas believes there is no reasonable justification to differentiate between utility investments that are similar in nature and provide similar cost and benefit to ratepayers solely based on mere ownership."

ComEd, NSG/PGL, and AIC all make similar arguments.

A separate argument against different ratemaking treatments for cloud-based and on-premise software is that treating cloud-based software as an operating expense does not reflect the useful life of the tool and unreasonably puts all of the rate impact in one year for a computing arrangement that may provide multiple years of benefit. An example of this argument is in NSG/PGL's comments:

> "For customers, the rate impact associated with recovery of capital assets is more even and better matched with the life of the asset. That is, rates

> reflect a return on and of the asset over its life. By contrast, the proper rate treatment of an expense item is to add the amount to rates at the level incurred or to be incurred in a test year. Rather than being spread over the asset life, customer rates would reflect the full expense when incurred. For IT assets of the sort that are the subject of this inquiry, asset / capital treatment is sound ratemaking because the resulting rates would better match the recovery with the customers' benefits from the used and useful period of the asset."

AIC makes a similar argument in their comments.

Fourth, the majority of utilities propose simple fixes to correct this ratemaking imbalance. ComEd, NSG/PGL, Nicor Gas, and AIC all agree with the Joint Software Provider Parties that most if not all of the costs of cloud-based software could be included in Account 303, "Miscellaneous Intangible Plant." NSG/PGL's comments are a good example of this argument, where they write,

> "NSG/PGL support treating investments in cloud computing solutions as "intangible plant" (account 303). The benefit of this treatment is that it places identical investments (cloud and on premises solutions) on equal footing. It removes the rate incentive for an on-premises solution and means that a cost benefit analysis of different computing solutions would be indifferent to the rate implications. Notably, this change would not create an incentive to choose a cloud solution; it would just eliminate the rate bias in favor of an on-premises solution. Consequently, NSG/PGL did not identify any costs of this approach. Like any investment, inclusion in rate base and recovery of a return on and of the investment would be subject to review in rate cases. A Commission order would be sufficient to implement the policy."

Some of these utilities did provide alternative suggestions, including accounting for cloud-based software as a capital lease, creating a new rider, or creating a regulatory asset. While each of these alternatives may achieve a more equal treatment of cloud-based and on-premise IT assets, the Joint Software Provider Parties are impressed that each of these utilities came to the same conclusion on Account 303. The Joint Software Provider Parties encourage the Commission to give extra consideration to this recommendation made by four utilities.

Most of the utilities include a request for specific Commission action to clarify the preferred ratemaking treatment. Both AIC and NSG/PGL recommend that the Commission issue an order. The Joint Software Provider Parties consider such an order a reasonable approach. Rulemaking may be overly burdensome for both the Commission and interested parties, especially given the simplicity of a possible fix (that is, simply instructing utilities to include the costs of cloud-based software in Account 303). At the same time, the Commission must take formal action so that there is no doubt about what the correct ratemaking treatment is, either for utilities or for interested parties. An order appears to strike the right balance.

The Joint Software Provider Parties note that another regulatory commission recently addressed the issue of accounting for cloud-based software in an order. On May 19, the New York Public Service Commission ("New York PSC") issued an "Order Adopting a Ratemaking and Utility Revenue Model Policy Framework" as part of the Reforming the Energy Vision proceeding. In this order, they write:

> "Utilities can earn a return on some types of REV-related operating investments within the current accounting system. Numerous IT applications will need to be developed and implemented. Rather than developing their own software, many businesses find it more efficient to enter contracts to lease software services over extended periods, typically three to five years. To the extent that these leases are prepaid, the unamortized balance of the prepayment can be included in rate base and earn a return. As utilities evaluate whether to purchase or lease these

applications, their ability to earn a return on a portion of the lease investment should help to eliminate any capital bias that could affect that decision."

The Joint Software Provider Parties encourage the Commission to take action similar to the New York PSC and issue simple guidance that clarifies how utilities can earn a rate of return on cloud-based software.

Finally, the Joint Software Provider Parties want to highlight some additional comments. First, the Joint Software Provider Parties note that MidAmerican Energy Company ("MidAmerican") differs from the other utilities on some points. MidAmerican did not highlight any specific ratemaking barriers, but encouraged the Commission to take up specific issues on a case-by-case basis. The Commission should feel comfortable that the great majority of utility parties support changes to ratemaking, and that none oppose it. Second, C3, Inc. and the Utility Analytics Institute both agree with the majority of parties that current ratemaking treatment is a barrier that must be addressed, and there is a need to "level the playing field."

The Joint Software Provider Parties appreciate the opportunity to comment in this Notice of Inquiry.

Dated: May 27, 2016

III. Contact Information

J.R. Tolbert
Advanced Energy Economy Institute
1000 Vermont Ave NW, Third Floor
Washington, DC 20009
jtolbert@aee.net

Laura Kier
Senior Associate, Market Operations

EnergyHub
232 3rd St C201
Brooklyn, NY 11215
kier@energyhub.net

Jake Oster
EnergySavvy
159 South Jackson St, Ste 420
Seattle WA, 98104
Jake@energysavvy.com

Greg Poulos,
Director, Regulatory Affairs
EnerNOC, Inc,
P.O. Box 29492
Columbus, OH 43229
gpoulos@enernoc.com

Brian Bowen
Regulatory Affairs Manager
FirstFuel Software, Inc.
18 S Michigan Ave, 12th Floor
Chicago, IL 60603
bbowen@firstfuel.com

Mathias Bell
Manager, Regulatory Affairs
Opower, Inc.
1515 North Courthouse Road
Arlington, VA 22201
Email: mathias.bell@opower.com

Merissa Khachigian
Director
Oracle, Inc.
State Government Affairs
merissa.khachigian@oracle.com

Bonnie Datta
Principal, Regulatory Affairs and Business Consulting

Siemens, Inc.
bonnie.datta.ext@siemens.com